

FINA1221 REVIEW

Corporations, Governance, Goals, Financial Markets, Institutions

- What are four common business structures?
Sole trader, partnership, private company, public/listed company
- What should be the goal of a financial manager?
Maximize the wealth of owners (long term interests)
- What is the agency problem? How do we reduce it?
As managers, their duty is to do the right thing to the owners; but have conflicts, maybe or not in the interest of owners.
Align the interests with the owners
 - Pay them partly in shares or options
 - Compete with one another to have the best geographical region to manage
- Why do we have financial markets?
Finite lives -> sell the company when retire, divide into pieces
Freedom to sell
- What are primary and secondary markets?
Issue the share receive the money, receive the book value/equity
Investor sells to some other investor
- What are financial intermediaries?
Go middle between you and other parties
Earn their cut in the middle
- How do financial intermediaries compare with financial markets?
Sit in the middle, deal with them not the outside
Commercial banks
 - Investment banks – align you up with another party; contract then out
 - To set up the contracts

Linking Accounting and Finance and Taxation

- Recap of accounting terminology:
What are assets, liabilities, and equity?
What are balance sheets, income statements, and cash flow statements?
- How does depreciation work for tax purposes?
Two type
 - For accounting purpose: accurate
 - For tax purposes (we interest in): cash flow. Deduct a greater amount. Tax deductive.
 - Capital gain when sell with lower book value/early
- What are written down values and book values?
100->90 y1 book value
Sell for 930
Gain 30 & pay tax on the 30
- How is capital gains tax calculated?
See above
- Why does Australia have a franking (imputation) system on dividends? How does it work?
Double taxation when you own the company

100 company pay 30 left 70

Pay dividend 70 + franking credit 30 = earn 100

Receive 30 - Tax rate * 100 (high tax payer pay more)

- How is income tax calculated? (company and personal marginal rates)

Time Value of Money

- What are EARs, APRs, and effective rates for holding periods?

Effective annual rate, annual percentage rate

Convert to the EAR

e.g. if your bank offers you a loan at 6% pa with monthly compounding, what is the effective monthly rate?

6%? Effective or nominal?

Two time frames -> nominal, not the truth

8% per year -> effective

0.5% per month

- How does time value of money work?

e.g. if \$300 grows to \$320 in 6 months, what is the annual interest rate?

- What is a perpetuity?

e.g. if a company has earnings of \$1M per year and your discount rate is 8% pa, what do you think the company is worth?

- What is an annuity?

e.g. if you take out a 3-year \$10,000 car loan at 10%pa with monthly repayments, how much do you pay per month?

nominal

- What is amortisation?

e.g. if you take out the 3-year car loan as above, how much is amortised in each of the first two months?

- What is arbitrage and how does it help financial markets?

Over price

Sell one buy one

Bonds

- What are coupon payments and face value?

Coupon rate \neq

- How much is paid when the bond is issued in the primary market?

How the market value the bond

No necessarily the face value

- What is a zero-coupon bond?

All the coupons have been removed

- What is yield? (to maturity)

=IRR

Buy a bond for x

Different cash flow coming back

- How are bond prices affected by interest rate movements?